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United States of America

PHILIPPINE ISLANDS

In the Supreme Court of the Philippine Islands

COMPANIA GENERAL DE TABACOS DE FILIPINAS,
Plaintiff-Appellee,
VERSUS
COLLECTOR OF INTERNAL REVENUE,
Defendant-Appellant.

G. R. No. 27766

(Appellate Jurisdiction)

ON PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE PHILIPPINE ISLANDS

Be it remembered that on the dates respectively mentioned the following proceedings were had in the above-entitled case:

On October 17, 1925, the plaintiff, by its attorneys, filed in the Court of First Instance of the City of Manila,

a complaint against the defendant which reads as follows:

[CAPTION OMITTED]

COMPLAINT

Plaintiff alleges:

I

That it is a corporation duly organized and existing under the laws of the Kingdom of Spain, duly licensed to do business in the Philippine Islands, and maintaining its principal office in said Islands in the City of Manila.

II

That the defendant is the duly appointed, qualified, and acting Collector of Internal Revenue for the Philippine Islands.

III

That during the year 1922 plaintiff exported from the Philippine Islands and sold in the United States of America certain quantities of centrifugal sugar, at a profit to it of P114,226.80 and certain quantities of manufactured tobacco at a profit to it of P296,341.19, a total profit to plaintiff of P410,567.99, Philippine currency.

IV

That the defendant, Collector of Internal Revenue, acting and pretending to act under the provi-

sions of Act 2833, as amended by Act 2926 (Philippine Income Tax Law), unlawfully and illegally did levy and assess against plaintiff a tax of three per centum on the amount of the aforesaid profits earned by plaintiff upon the merchandise exported and sold by it in the United States of America during the year 1922, as alleged in Paragraph III hereof, in the sum of P12,009.75, Philippine currency.

V

That on the 18th day of October, 1923, plaintiff, in order to avoid the infliction upon it of severe fines and penalties and the distraint of its property by defendant, did pay to defendant, under instant protest in writing, the said sum of P12,009.75, Philippine currency.

VI

That plaintiff's protest against the aforesaid tax was based upon the grounds:

(a) That the profit obtained by plaintiff, from the sugar and tobacco sold by it in the United States of America during the year 1922, as aforesaid, was subject to the income tax levied by the Federal Government of the United States, under the United States Revenue Act of 1921, only, as profits derived from sources within the United States by foreign corporations; and

(b) That no part of the profit obtained by plaintiff, from the sugar and tobacco sold by it in the United States of America during the year 1922,

as aforesaid, was derived from sources within the Philippine Islands.

VII

That plaintiff's protest against the payment of the aforesaid tax was overruled and denied by defendant on the 20th day of October, 1923, and defendant has refused, and still continues in his refusal, to return to plaintiff, on demand, the said sum of ₱12,009.75, Philippine currency, or any part thereof.

Wherefore, plaintiff prays judgment against defendant for the sum of ₱12,009.75, Philippine currency, and costs.

Manila, P. I., October 17, 1925.

FISHER, DEWITT, PERKINS & BRADY,
BY: JOHN R. MCFIE, JR.
Attorneys for Plaintiff.

On November 18, 1925, the defendant Collector of Internal Revenue filed an answer to the foregoing complaint as follows:

[CAPTION OMITTED]

ANSWER

Now comes the defendant in the above-entitled case and through his undersigned attorney to this court respectfully states:

I

That he denies each and every allegation contained in each and every paragraph of the plaintiff's complaint except what is specifically admitted herein.

II

That he admits the allegations contained in Paragraphs I, II, III, and V of plaintiff's complaint except that the amount upon which the income tax assessed and collected from the plaintiff is not on the total of those profits stated in Paragraph III of the complaint, namely, the ₱114,226.80 and the ₱296,341.19, but upon the total of these two amounts minus ₱10,243.14, representing losses sustained by the plaintiff in certain quantities of oil and copra exported from the Philippine Islands and sold in the United States during the year 1922.

III

That the taxes mentioned in the plaintiff's complaint and sought to be recovered by it in this case were lawfully and legally levied, assessed, and collected under provisions of Act 2833, as amended by Act 2926.

IV

Wherefore, the defendant prays the court to render judgment that plaintiff take nothing by its

complaint, with costs of this action against plaintiff.

Manila, November 16, 1925.

DELFIN JARANILLA
Attorney-General.

On January 22, 1926, the plaintiff filed the following amended complaint:

[CAPTION OMITTED]

AMENDED COMPLAINT

Plaintiff alleges:

I

That it is a corporation duly organized and existing under the laws of the Kingdom of Spain, duly licensed to do business in the Philippine Islands, and maintaining its principal office in said Islands in the City of Manila.

II

That the defendant is the duly appointed, qualified, and acting Collector of Internal Revenue for the Philippine Islands.

III

That during the year 1922 plaintiff exported from the Philippine Islands and sold in the United

States of America certain quantities of centrifugal sugar, manufactured tobacco, copra, and coconut oil, at a net profit to plaintiff of ₱400,324.85, Philippine currency.

IV

That the defendant, Collector of Internal Revenue, acting and pretending to act under the provisions of Act 2833, as amended by Act 2926 (Philippine Income Tax Law), unlawfully and illegally did levy and assess against plaintiff a tax of three per centum on the amount of the aforesaid net profits earned by plaitiff upon the merchandise exported and sold by it in the United States of America during the year 1922, as alleged in paragraph III hereof, in the sum of ₱12,009.75, Philippine currency.

V

That on the 18th day of October, 1923, plaintiff, in order to avoid the infliction upon it of severe fines and penalties and the distraint of its property by defendant, did pay to defendant, under instant protest in writing, the said sum of ₱12,009.75, Philippine currency.

VI

That plaintiff's protest against the payment of the aforesaid tax was overruled and denied by defendant on the 20th day of October, 1923, and defendant has refused and still continues in his refusal, to return to plantiff, on demand the said sum of

P12,009.75, Philippine currency, or any part thereof.

Wherefore, plaintiff prays judgment against defendant for the return to it of the sum of P12,009.75, Philippine currency, and costs.

Manila, P. I., January 22, 1926.

FISHER, DEWITT, PERKINS & BRADY,
By: JOHN R. MCFIE, JR.,
Attorneys for Plaintiff,
601 Pacific Building, Manila.

On June 12, 1926, the plaintiff and the defendant filed the following agreed statement of facts:

[CAPTION OMITTED]

AGREED STATEMENT OF FACTS

Come now the parties, plaintiff and defendant, in the above-entitled cause, by their undersigned attorneys, and respectfully submit to this Honorable Court the following statement of facts, which the court may find as true and enter judgment thereon:

I

That plaintiff is a corporation duly organized and existing under the laws of the Kingdom of Spain duly licensed to do business in the Philippine Islands, and maintaining its principal office in said Islands in the City of Manila.

II

That defendant is the duly appointed, qualified, and acting Collector of Internal Revenue for the Philippine Islands.

III

That plaintiff is the owner of several "haciendas," sugar and oil mills and tobacco factories located in the Philippine Islands destined to the production or manufacture of tobacco, sugar, copra, and coconut oil for sale therein and in foreign countries; and has been and is still engaged, in the Philippine Islands, in the shipping business and in the buying and selling of tobacco, sugar, copra, and oil and in the exportation of the same, and that its business has been, and is being done mainly in the Philppine Islands.

IV

That the Philippine branch of the plaintiff corporartion on various dates during the year 1922 exported from the Philippine Islands a quantity of centrifugal sugar, of which ten per centum was produced and ninety purchased by it in the Philippine Islands, and which was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch; and that from such transactions on centrifugal sugar during said year 1922, the plaintiff made a profit of P114,226.80, Philippine currency.

V

That, likewise, the plaintiff's Philippine branch on various dates during said year 1922, exported from the Philippine Islands a certain quantity of manufactured tobacco produced by it in the Philippine Islands which was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being likewise subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch, deriving from such transactions a profit of ₱296,341.19, Philippine currency.

VI

That, likewise, the plaintiff's Philippine branch on various dates during the said year 1922, exported from the Philippine Islands a certain quantity of copra and a certain quantity of coconut oil, produced, purchased, or manufactured by it in the Philippine Islands, which were sold in the United States by the agency therein of the plaintiff's Philippine branch, such sales being likewise subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch, and that from such transactions on copra and coconut oil the plaintiff suffered losses amounting to ₱10,243.14, Philippine currency.

VII

That deducting the sum of ₱10,243.14, the losses mentioned in Paragraph VI of this stipulation

from the sum of ₱410,567.99, the aggregate of the profits mentioned in Paragraphs IV and V, there remained a net profit of ₱400,324.85.

VIII

That the said net profit of ₱400,324.85, together with other gains, profits, or income were accounted for by the plaintiff on its books of accounts kept in the Philippine Islands as earnings made by and accruing to the Philippine branch, thereby subjecting such profits, gains, or incomes to further business deductions—management expenses, losses, etc.

IX

That the defendant Collector of Internal Revenue, acting and pretending to act under the provisions of Act 2833 (Philippine Income Tax Law), as amended by Act 2926, levied and assessed against plaintiff a tax of three (3) per centum on the amount of the aforesaid net profits (₱400,324.85) earned by plaintiff, as recited in Paragraphs IV, V and VI thereof, in the sum of ₱12,009.75, Philippine currency.

X

That on the 18th day of October, 1923, plaintiff, in order to avoid the infliction upon it of fines and penalties and the distraint of its property by defendant, did pay to defendant, under instant protest in writing, the said sum of ₱12,009.75, Philippine currency.

XI

That plaintiff's protest against the payment of the aforesaid tax was overruled and denied by defendant on the 20th day of October, 1923, and defendant has refused, and still continues in his refusal, to return to plaintiff, on demand, the said sum of ₱12,009.75, Philippine currency, or any part thereof.

XII

That the parties hereto reserve the right to introduce evidence, direct or rebuttal, on any point not herein stipulated and which may be deemed material and necessary for the proper determination of this case.

Manila, P. I., June 12, 1926.

Respectfully submitted,

FISHER, DEWITT, PERKINS & BRADY,
By: WILLIAM C. BRADY,
Attorneys for Plaintiff.
DELFIN JARANILLA,
Attorney-General,
Attorney for Defendant.

On November 16, 1926, the Court of First Instance of the City of Manila rendered its decision as follows:

[CAPTION OMITTED]

DECISION

According to the agreed statement of facts attached to the record, the Compañía General de Tabacos de Filipinas, which is a corporation duly organized under the laws of the Kingdom of Spain, with license to do business in these Islands, having its principal office in this City of Manila, being the owner of several sugar estates, oil mills and tobacco factories situated in these Islands and devoted to the production and manufacture of tobacco, sugar, copra and coconut oil to be sold here and abroad, exported in the year 1922 from these Islands a certain amount of centrifugal sugar of which ten per cent was produced and ninety per cent bought in these Islands but sold in the United States through the agency of the branch of the plaintiff corporation, which sale was made with the approval of the branch in these Islands as regards the price and other terms and conditions thereof, and produced a gain of ₱114,226.80, Philippine currency.

That in the same year, but on different dates, said corporation exported a certain amount of tobacco manufactured and produced by itself in these Islands to the United States where it was sold by the agency of the branch obtaining a profit of ₱296,241.19.

In the same year, the same corporation exported to the United States certain amount of copra and oil, which was sold in the same manner and conditions, causing a loss of ₱10,243.14, instead of gain, which loss reduced the total amount of the two gains above mentioned to a net profit of ₱400,324.85, upon which the defendant Collector of Internal Revenue, under the provisions of Act No. 2833, concerning internal revenue taxes, as amended by Act No. 2926, collected from the plaintiff corporation as three per cent tax upon the amount last mentioned, the sum of ₱12,009.75, which the plaintiff corporation, found it necessary to pay, although it did not consider itself bound to do so, under protest, in order to avoid the imposition of the fines and other penalties prescribed by the law.

The refund of said amount is claimed in the complaint that initiated this action.

The only question to be decided is, in view of the facts drawn from the agreed statement of facts, a legal one, and that is whether or not under section 10 of the Act first cited, as amended by section 7 of Act No. 2926, the plaintiff corporation is bound to pay the tax collected from it.

Said section 10, in providing the collection of a tax of three per cent upon the total amount of the net income received during the preceding civil year by every corporation, joint stock company, partnership, joint account association, insurance company organized, authorized or existing under the laws of any foreign country, determines the source from

which it must come and the place within which it must exist, and that place, according to said section, is the Philippine Islands.

Counsel for defendant, in interpreting the words used by the law, to wit, "sources within the Philippine Islands," states that the income or benefit of the plaintiff corporation upon which the defendant has collected the three per cent tax, *was obtained from articles which were produced, manufactured or purchased in the Philippine Islands*, and the sale of which, while it took place in the United States, has been subject to the confirmation and absolute control of the branch of the plaintiff corporation in these Islands and that the profits realized were credited on the books of account of the said branch; and he concludes that, this being the case, the income or profit above mentioned was an income obtained from sources within the Philippine Islands.

The court is of the opinion that the interpretation is not correct. While the goods and merchandise mentioned in the agreed statement of facts are considered as sources of income, because it is from them, once sold, exchanged or assigned in payment of a debt, that the incomes proceed, yet said source must be considered remote for the purposes of the assessment of the tax provided in the section of said law which virtually makes a distinction, according as the merchandise has been sold in these Islands, or outside thereof.

If the merchandise were sold within these Islands, the foreign corporation, owner of the same,

is of course subject to the payment of the tax demanded of it, because the receipt or income was obtained from a sale made in this city. But if it is sold, as is the case here, in the United States, the three per cent tax cannot be levied upon the income obtained, in the opinion of the court.

The true source of the income received by the plaintiff corporation, for the purposes of the application of the law, is not the merchandise itself, but the transaction made concerning it, because so long as the merchandise is not placed on the market and remains stored or deposited in these Islands, they cannot mean any real income, nor net income subject to tax. A private merchant or a corporation and other individuals pertaining to other professions pay the income tax when the same has been obtained as income from the sale of any merchandise, or the practice of a particular profession, or any other kind of activity.

If the goods mentioned, although produced in these Islands, could not have been coverted into cash or receipts representing income but after they are sold in the United States, the income that must be subject to tax, according to said law, was derived from sources which are not within the Philippine Islands, but in the United States, because said sources are not the goods produced here, but the sale thereof made in America.

This is the genuine meaning of the section of the law in question, because if it were as maintained by counsel for the defendant, the words used by the

law "sources within the Philippine Islands" would be of no use, for the simple reason that if they are to be held to mean goods produced or manufactured in the United States and sold in that continent, it is clear that the merchant or corporation owner and seller thereof is not bound to pay in these Islands any tax upon the income obtained.

It is, therefore, evident that in using the words above italicized, the law means a transaction effected here, and not in the United States, of articles produced or manufactured here or in foreign countries, but purchased and brought here and resold in these Islands. If they are sold in the United States, although they are goods produced and manufactured here, as in the case before us, the receipts obtained from the transactions or sales effected outside of these Islands cannot be subject to the three per cent tax on income.

Such is the spirit of the law, the purpose of which must be the encouragement of mercantile spirit and initiative, not only among the natives, but also among the foreigners, because it constitutes one of the true sources of wealth and agrandizement of this country, to the welfare and happiness of whose inhabitants, every sound and wise legislation must tend. To place the merchants, whether natives or foreigners, who are cooperating towards the material development of the Philippine country, in a situation to pay double income tax, one in these Islands and another in those points where the national products are sold, is not to encourage commerce, nor to work for the benefit of the taxpaying people.

The Collector of Internal Revenue is sentenced to refund to the Compañía General de Tabacos de Filipinas the sum of ₱12,009.75, without special finding as to costs.

Manila, November 16, 1926.

S. DEL ROSARIO
Judge.

On December 15, 1926, the defendant filed the following:

[CAPTION OMITTED]

EXCEPTION AND MOTION FOR NEW TRIAL

Now comes the defendant, by his undersigned attorney, and excepts to the decision rendered in the above-entitled case on November 16, 1926, of which decision, the undersigned was notified on November 22, 1926, and moves this court to set aside the judgment rendered therein and grant a new trial of said action for the following reasons:

1. That the evidence presented does not justify the decision.

2. That the decision is contrary to law.

Manila, December 15, 1926.

DELFIN JARANILLA,
Attorney-General,
Attorney for Defendant.

On December 31, 1926, the Court of First Instance entered an order denying the foregoing motion for new trial filed by the defendant, and on January 17, 1927, the defendant filed the corresponding exception thereto and announced his intention to appeal to the Supreme Court by bill of exceptions.

On January 27, 1927, and within the time limited by law, the defendant filed in the Court of First Instance his bill of exceptions, requesting that it be approved, and transmitted to the Supreme Court of the Philippine Islands together with all the evidence presented, oral or documentary.

On April 2, 1927, the Court of First Instance approved, signed and certified the said bill of exceptions, and the same was, on April 27, 1927, transmitted to the Supreme Court of the Philippine Islands for the purposes of the appeal.

On April 30, 1927, the bill of exceptions was docketed on appeal without fees, the case being duly registered on appeal under No. 27766 of the docket of the Supreme Court of the Philippine Islands.

On May 25, 1927, the bill of exceptions was printed and filed.

On July 15, 1927, the defendant and appellant Collector of Internal Revenue filed his brief in the case, assigning the following errors:

[CAPTION OMITTED]

ASSIGNMENT OF ERRORS

I

The lower court erred in declaring that the plaintiff's income taxed by the defendant was re-

ceived from sources not within the Philippine Islands and therefore not subject to taxation.

II

The lower court erred in condemning the defendant to return to the plaintiff the sum of ₱12,009.75, amount of the tax in question, instead of dismissing the complaint.

III

The lower court erred in not granting a new trial.

On September 8, 1927, the plaintiff and appellee, Compañía General de Tabacos de Filipinas, filed its brief in the case.

On September 27, 1927, the case was submitted to the Supreme court for decision on the merits.

On December 6, 1927, the Supreme Court rendered its decision in the case, in the words and figures following, to-wit:

[CAPTION OMITTED]

DECISION

STATEMENT

Plaintiff is a corporation organized and existing under the laws of the Kingdom of Spain, duly licensed to transact business in the Philippine Islands, with its principal office in the City of Manila. The defendant is the Collector of Internal Revenue.

Plaintiff alleges that during the year 1922 it exported from the Philippine Islands and sold in the United States certain quantities of centrifugal sugar, manufactured tobacco, copra and coconut oil, at a net profit of ₱400,324.85. That the defendant, acting and pretending to act under the provisions of Act No. 2833, as amended by Act No. 2926, unlawfully and illegaly levied and assessed against the plaintiff a tax of three per centum on the amount of such profit during the year 1922 amounting to ₱12,009.75, which plaintiff paid under written protest on the ground that the profit which it obtained from the sugar and tobacco sold by it in the United States was subject to the income tax levied by the government of that country. That no part of plaintiff's profit was derived from sources within the Philippine Islands. That plaintiff's protest was overruled and denied, and defendant has refused to return the amount of such tax. Wherefore, it prays for a corresponding judgment, with costs.

For answer the defendant made a general and specific denial of all of the material allegations of the complaint, except that which is specifically admitted. Defendant admits paragraphs 1, 2, 3, and 5 of plaintiff's complaint, except as to the amounts, and alleges that the taxes which plaintiff seeks to recover were lawfully levied, assessed and collected under the provisions of Act No. 2833, as amended by Act No. 2926, and defendant prays that plaintiff's complaint be dismissed, with costs.

The case was tried and submitted upon the following "Agreed Statement of Facts":

"I

"That plaintiff is a corporation duly organized and existing under the laws of the Kingdom of Spain, duly licensed to do business in the Philippine Islands, and maintaining its principal office in said Islands in the City of Manila.

"II

"That defendant is the duly appinted, qualified, and acting Collector of Internal Revenue for the Philippine Islands.

"III

"That plaintiff is the owner of several 'haciendas', sugar and oil mills and tobacco factories located in the Philippine Islands destined to the production or manufacture of tobacco, sugar, copra, and coconut oil for sale therein and in foreign countries; and has been and is still engaged, in the Philippine Islands, in the shipping business and in the buying and selling of tobacco, sugar, copra, and oil and in the exportation of the same, and that its business has been, and is being done mainly in the Philippine Islands.

"IV

"That the Philippine branch of the plaintiff corporation on various dates during the year 1922

exported from the Philippine Islands a quantity of centrifugal sugar, of which ten per centum was produced and ninety purchased by it in the Philippine Islands, and which was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch; and that from such transactions on centrifugal sugar during said year 1922, the plaintiff made a profit of ₱114,226.80, Philippine currency.

"V

"That, likewise, the plaintiff's Philippine branch on various dates during said year 1922, exported from the Philippine Islands a certain quantity of manufactured tobacco produced by it in the Philippine Islands, which was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being likewise subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch, deriving from such transactions a profit of ₱296,341.19, Philippine currency.

"VI

"That, likewise, the plaintiff's Philippine branch on various dates during the said year 1922, exported from the Philippine Islands a certain quantity of copra and a certain quantity of coconut

oil, produced, purchased, or manufactured by it in the Philippine Islands, which were sold in the United States, by the agency therein of the plaintiff's Philippine branch, such sales being likewise subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch, and that from such transactions on copra and coconut oil the plaintiff suffered losses amounting to P10,243.14, Philippine currency.

"VII

"That deducting the sum of P10,243.14, the losses mentioned in paragraph VI of this stipulation, from the sum of P410,567.99, the aggregate of the profits mentioned in Paragraphs IV and V, there remained a net profit of P400,324.85.

"VIII

"That the said net profit of P400,324.85, together with other gains, profits, or income were accounted for by the plaintiff on its books of accounts kept in the Philippine Islands as earnings made by and accruing to the Philippine branch, thereby subjecting such profits, gains, or incomes to further business deductions—management expenses, losses, etc.

"IX

"That the defendant Collector of Internal Revenue, acting and pretending to act under the pro-

visions of Act 2833 (Philippine Income Tax Law), as amended by Act 2926, levied and assessed against plaintif a tax of three (3) per centum on the amount of the aforesaid net profits (₱400,324.85) earned by plaintiff, as recited in Paragraps IV, V, and VI hereof, in the sum of ₱12,009.75, Philippine currency.

"X

"That on the 18th day of October, 1923, plaintiff, in order to avoid the infliction upon it of fines and penalties and the distraint of its property by defendant, did pay to defendant, under instant protest in writing, the said sum of ₱12,009.75, Philippine currency.

"XI

"That plaintiff's protest against the payment of the aforesaid tax was overruled and denied by defendant on the 20th day of October, 1923, and defendant has refused, and still continues in his refusal, to return to plaintiff, on demand, the said sum of ₱12,009.75, Philippine currency, or any part thereof.

"XII

"That the parties hereto reserve the right to introduce evidence, direct or rebuttal, on any point not herein stipulated and which may be deemed material and necessary, for the proper determination of this case."

Upon such issues and stipulated facts, the

lower court rendered judgment for the plaintiff as prayed for in its complaint, without costs, to which the defendant duly excepted and filed a motion for a new trial, which was overruled. On appeal the defendant assigns the following errors:

"I

"The lower court erred in declaring that the plaintiff's income taxed by the defendant was received from sources not within the Philippine Islands and therefore not subject to taxation.

"II

"The lower court erred in condemning the defendant to return to the plaintiff the sum of ₱12,009.75, amount of the tax in question, instead of dismissing the complaint.

"III

"The lower court erred in not granting a new trial."

JOHNS, *J.*:

Upon the stipulation of facts, the question involved of this appeal is the legal construction to be placed on Section 10 of Act No. 2833, as amended by Section 7 of Act No. 2926, which provides as follows:

"There shall be levied, assessed, collected, and paid anually upon the total net income received in

the preceding calendar year from all sources by every corporation, joint-stock company, partnership, joint-account (cuenta en participación), association, or insurance company, organized in the Philippine Islands, no matter how created or organized, but not including duly registered general copartnerships (compañías colectivas), a tax of three per centum upon such income received in the preceding calendar year assessed, collected, and paid annually upon the total net income received in the preceding calendar year from all sources within the Philippine Islands by every corporation, joint-stock company, partnership, joint-account (cuenta en participación), association, or insurance company, organized, authorized, or existing under the laws of any foreign country, including interest on bonds, notes, or other interest bearing obligations of residents, corporate or otherwise, and including the income derived from dividends or net profits subject to the tax established in this subsection."

In its final analysis, that question involves the legal meaning and construction to be placed on the words "sources within the Philippine Islands," as they are used in that section, in connection with, and founded upon, the stipulation of facts. It will be noted that the section above quoted has two separate and distinct provisions; one for a tax of three per centum for each calendar year on the annual total net income derived from all sources by a domestic corporation, and the other for a like tax "upon the tatal net income received in the preceding calendar

year from all sources within the Philippine Islands" by any corporation organized and "existing under the laws of any foreign country."

It is very apparent that it was the purpose and intent of the Legislature that a foreign corporation which has a branch office in the Philippine Islands and engaged in business here should pay the same amount of income tax on that business as a domestic corporation would have to pay; otherwise, a foreign corporation with a branch office in the Philippines and doing business here would have an advantage of the amount of such annual income tax over a domestic corporation engaged in the same line of business.

Under paragraph 4 of the agreed statement of facts, it is stipulated that during the year 1922, plaintiff exported from the Philippine Islands a quantity of centrifugal sugar, of which ten per centum was produced and ninety purchased by it in the Philippine Islands, and which was sold in the United States by and through the agent of the plaintiff's Philippine branch, and that the sale was subject to confirmation and absolute control as to price and other terms and conditions by the plaintiff's Philippine branch. The same stipulation is made as to the tobacco, copra and coconut oil mentioned and described in the complaint. It is further stipulated that the profits or incomes in question were accounted for by the plaintiff on its books of account "kept in the Philippine Islands as earnings made by and accruing to the Philippine branch, etc." That is to

say, that although the sales of the products from which the incomes in question were derived were made in the United States, they were made there by an agent of the Philippine branch of the plaintiff, and all of them were made subject to the confirmation and absolute control as to price, terms and conditions by the plaintiff's Philippine branch. In other words, no sale was actually consummated until after it was ratified and approved by the local branch, and all profits or incomes from such sales were accounted for by the plaintiff on its books kept in the Philippine Islands "as earnings made by and accruing to the Philippine branch." It is further stipulated that the sugar, tobacco, copra and coconut oil in question, from which the net incomes were derived, were exclusively the products of the Philippine Islands in which and where they were produced on the properties of the plaintiff or by it purchased at or through its branch office in the Philippines, and from which country they were shipped to the United States and there sold in the same form and condition as when they were shipped from the Philippine Islands. That is to say, the income in question was derived and received by the plaintiff from the exclusive products of the Philippine Islands which were purchased or produced by and through its branch office in the Philippine Islands and which it shipped from the Islands to the United States, where such products were sold in the identical condition in which they were shipped from the Philippine Islands. Hence, it must follow that the net income of the plaintiff as to such products was

from "sources within the Philippine Islands" where the products were purchased or produced and where the plaintiff maintains its branch office for that specific purpose.

The appellee cites and relies upon the following opinion of the Attorney-General of the United States:

"A corporation organized under the laws of Scotland owns and operates two sawmills in the United States. The mills saw logs into plank squares called 'handle blanks' and also roughly turn hammer handles. These products are exported to Glasgow where they are finished at the home mill. In addition the manager of the American plant buys logs in the United States and exports them as such to Great Britain. No part of the products of the mills located in this country or of the logs purchased here is sold in the United States, but the entire output is sold in Great Britain. The plants and operations of the manager in the United States are conducted solely from fund sent to this country from the home office in Glasgow, Scotland, and no funds are sent to the home office from the American plants."

Based upon such facts, the Attorney-General held that the Scotland corporation was not liable to the tax in question. Assuming that to be the law, there is a very marked distinction between the facts in that case and the stipulated facts in this case. There the two sawmills in the United States sawed logs into plank squares called "handle blanks" and

also "roughly turn hammer handles." In that condition, they were shipped to Glasgow where "they were there finished at the home mill" and then placed on the market. It further appears that all of the operations in the United States "are conducted solely from funds sent to this country from the home office in Glasgow, Scotland, and no funds are sent to the home office from the American plants." In the instant case, it is stipulated that the plaintiff exported the products in question from the Philippine Islands to the United States where they were sold by an agency of the plaintiff's Philippine branch, and that such sale was "subject to confirmation and absolute control as to price and other terms and conditions thereof by the plaintiff's Philippine branch", and that all of such net profits were kept and accounted for by the plaintiff "on its books of account kept in the Philippine Islands as earnings made by and accruing to the Philippine branch." That opinion is not in point upon the stipulated facts in this case.

Appellee's contention if sustained would give a preference to a foreign corporation doing business through a branch office in the Philippine Islands over a domestic corporation engaged in the same line of business to the amount of the 3% tax upon the income in question. That was not the purpose and intent of the Legislature. It is very apparent that the Legislature intended that a foreign corporation with a branch office in the Philippine Islands could do business here upon the same terms and con-

ditions as a domestic corporation, and that it never intended that a foreign corporation with a branch office and doing business in the Philippines should have any preference over a domestic corporation engaged in the same line of business.

In the instant case, the record is conclusive that all of the sources of plaintiff's income in question had their origin in or were derived from its branch office in the Philippine Islands by and through the products of the Philippine Islands, which were purchased or produced by its branch office in the Philippine Islands, and that all of the sales in question were made through its branch office, and that no sale was actually consummated until such time as it was approved by the branch office both as to terms and conditions, and that an account of all of such sales made in the United States was rendered to the branch office, together with the proceeds, where a full and complete record was kept and made of all of such transactions.

Plaintiff's source of income in question was from the products of the Philippine Islands which were derived through its branch office, and it appears from the stipulation of facts that all of such products when shipped by the branch office to the United States were there sold in the identical condition in which they were shipped from the Philippine Islands, and that an account of all of such sales was rendered to the branch office.

Upon the record, we are clearly of the opinion that upon the products in question, plaintiff's net

income was derived from "sources within the Philippine Islands."

The judgment of the lower court is reversed and the complaint dismissed, with costs for the defendant.

Ten days after the publication of this decision final judgment will be entered, and five days thereafter the record will be remanded to the court below.

It is so ordered.

(SGD.) CHARLES A. JOHNS

WE CONCUR—

(SGD.) RAMON AVANCENA
" THOS. A. STREET
" GEO A. MALCOM
" IGNACIO VILLAMOR
" JAMES A. OSTRAND
ANTONIO VILLA-REAL

JOHNSON, J.; RESERVED HIS VOTE.

On December 20, 1927, the plaintiff and appellee filed the following:

[CAPTION OMITTED]

MOTION FOR REHEARING

Come now the undersigned attorneys in representation of the plaintiff and appellee Compañia General de Tabacos de Filipinas and respectfully

move this Honorable Court to grant a rehearing in the above-entitled case, for the following reasons, to wit:

That the question involved is of public concern, affecting, as it does, the revenue of the Philippine government and the income of all mercantile and trading foreign corporations with branch offices in the Islands engaged in selling products of said Islands abroad.

That this Honorable Court has decided the case upon the theory that a foreign corporation with a branch office in the Philippines and doing business here would have an advantage of the amount of such annual income tax over a domestic corporation engaged in the same line of business. Thus the decision reads:

"It is very apparent that it was the purpose and intent of the Legislature that a foreign corporation which has a branch office in the Philippines and engaged in business here should pay the same amount of income tax on that business as a domestic corporation would have to pay; otherwise, a foreign corporation with a branch office in the Philippines and doing business here would have an advantage of the amount of such annual income tax over a domestic corporation engaged in the same line of business."

That while this theory at first glance seems reasonable and fair it is fundamentally erroneous and is at variance with and repugnant to the whole scheme of the income tax law, for foreign corpora-

tions and domestic corporations are not on the same footing for taxation purposes.

That the allowable deductions to foreign corporations are different from the allowable deductions to domestic corporations, and the law makes no distinction between a foreign corporation without a branch in the Islands and a foreign corporation with a branch in the Philippine Islands.

That foreign corporations are taxed only upon so much of their income as they receive from "all sources within the Philippine Islands", consequently their allowable deductions are correspondingly restricted.—Black—Income and other Fed. Taxes, p. 243.

That as a domestic corporation pays a tax upon the total net income received from all sources it may, in ascertaining its net income, deduct from the gross amount of its income all the ordinary and necessary expenses paid within the year in the maintenance of its business and properties, including rentals, pertaining to its agency in the United States.

That no such an allowance is permitted to a foreign corporation with a branch in the Philippine Islands, as in the case of a corporation *organized under the laws of a foreign country* the deduction is limited to expenses in connection with *its business and property*, including rentals for such property *within the Philippine Islands*. Sec. 12 (a) First; Sec. 12 (b) First.

That a domestic corporation is allowed a deduction for all losses actually sustained and charged off within the year, not compensated by insurance

or otherwise, while a corporation organized under the laws of a foreign country may only deduct losses as arise in connection with the business or trade conducted by it *within the Philippine Islands*, and *not* in connection with *business, or trade conducted by it* in the United States or elsewhere.

That a domestic corporation may deduct taxes paid within the year imposed by *any foreign government*. On the other hand, if in the case at bar the goods had been sold in England through plaintiff's agency there, taxes paid to the British government would not be allowable as a deduction, as no such deduction is permitted foreign corporations. Sec. 12 (a) Fourth; Sec. 12 (b) Fourth.

That it will thus be seen, if there is any question of "advantage", by the terms of this Honorable Courts's decision, a domestic corporation would have an advantage over a foreign corporation with a branch office in the Philippines and doing business here, to the extent of the differences allowed in favor of domestic corporations as against foreign corporations in the matter of allowable deductions.

That in the case of Kidd v. Alabama, 188 U. S. 730, at page 732, Mr. Justice Holmes said: "No doubt it would be a great advantage to the country and to the individual states if principles of taxation could be agreed upon which did not conflict with each other, and, a common scheme could be adopted by which taxation of substantially the same property in two jurisdictions could be avoided."

That this is why the 1916 Revenue Act (from which our statute has been copied) emphasizes the

source of income as the test of taxability, and this has been considered a long step in advance towards international comity in taxation. Holmes Fed. Taxes—Sixth Edition, page 398.

That the decision of this Honorable Court permits the very thing which it was the object of the law to avoid, to wit, double taxation, for although taxes paid to the United States government are allowable as a deduction, no such deduction is allowed when the taxes are paid elsewhere.

That when this Honorable Court says that a foreign corporation which has a branch office in the Philippines and engaged in business here should pay the same amount *of income tax on that business* as a domestic corporation would have to pay, this Honorable Court overlooks the fact that it is the receipt of income from "sources within the Philippine Islands" rather than *the doing of business within the Philippine Islands*, which is the test of taxability of foreign corporations. In other words, the law imposes an income tax, not an excise tax, on corporations, and there is no tax on the business. For instance, the Revenue Law of 1909 of the United States was an excise tax law, both with respect to domestic and foreign corporations, unassured with reference to net income.—Flint v. Stone—Tracy Co., 220., U. S. 107; Bryant & May Ltd. v. Scott, 226 Fed. 875; cited in Holmes Federal Taxes, Sixth Edition, p. 441.

That as the income derived from the transactions described in the instant case is taxable in the United States under the decisions and rulings of the

Treasury Department as being "income from sources within the United States" (32 Opinion, Atty. General of the United States 336; 5 Treasury Bulletin 1-39-519; Holmes Fed. Taxes 1923 Edition, p. 82; Holmes Fed. Taxes Sixth Edition; 34 Opinion, Atty. General of the United States 93), such income should not be considered in this jurisdiction as "income from sources within the Philippine Islands."

That the theory upon which this case has been decided, to use the language quoted by a distinguished member of this Honorable Court in the case of Compañia General de Tabacos de Filipinas versus Collector of Internal Revenue, G. R. 23400, amounts to an "invidious discrimination" against foreign corporations with branch offices doing business in the Philippine Islands; and

That the decision of this Honorable Court as it stands amounts to a violation of the uniformity clause of the Jones Law, because the difference in the deductions granted to domestic corporations and foreign corporations with branch office in Manila will not now correspond to and bear a reasonable relation to the difference in the base of the tax.

In conclusion, it will thus be seen that as a result of this Honorable Court's construction a different and much more onerous rule is applied by the Income Tax Law for foreign corporations than for domestic corporations engaged in business of exactly the same kind and character. This, we respectfully contend, constitutes a denial of the equal protection of the laws and is violative of the guaranties a af-

forded all persons within the Philippine Islands by the Jones Law. (Leecraft v. Texas Co. 231 Fed. 918; Southern R. Co. v. Greene, 216 U. S. 400, 54 L. Ed. 536.) The equal protection of the laws means subjection to equal laws applying alike to all in the same situation. If the plaintiff is a person within the jurisdiction of the Philippine Islands, and it is no longer open to discussion that it is (Pambina Consol. Mining etc., Co. v. Pennsylvania, 125 U. S. 181, 31 L. Ed. 650; Gulf, etc. R. Co., v. Ellis, 165 U. S. 150, 41 L. Ed. 666; Blake v. McCluy, 172 U. S. 239, 43 L. Ed. 432), it is entitled to stand before the law on equal terms, to enjoy the same rights as belong to, and to bear the same burdens as are imposed upon, all other persons in a like situation. Foreign corporations may not thus be arbitrarily discriminated against without any real or substantial basis therefore, such arbitrary selection not being justifiable as an exercise of the right of classification of the subjects of taxation (Gulf, etc. R. Co. v. Ellis, 165 U. S. 150, 41 L. Ed. 666; Cotting v. Kansas City Stock Yards Co., 183 U. S. 79, 46 L. Ed. 92; Connody v. Union Sewer Pipe Co., 184 U. S. 540, 559, 46 L. Ed. 679).

Manila, P. I., December 17, 1927.

Respectfully submitted,

DEWITT, PERKINS & BRADY,

By: WILLIAM C. BRADY,

Attorneys for the Compañia General de Tabacos de Filipinas.

On February 8, 1928, the Supreme Court of the Philippine Islands denied the foregoing motion in the following resolution, with Mr. Justice Johnson and Mr. Justice Street dissenting therefrom:

> "Considering the motion of the attorneys for the plantiff-appellee in case R. G. No. 27766, Compañia General de Tabacos de Filipinas vs. Collector of Internal Revenue, praying for the reasons given, that the decision heretofore rendered therein be reconsidered, the Court, sitting in banc, DENIED THE MOTION. Messrs. Justices Johnson and Street dissented upon the grounds set forth in their separate opinions filed therein."

The respective dissenting opinions of Messrs. Justices Johnson and Street read as follows:

JOHNSON, *J., dissenting*:

At the time this case was considered and voted I reserved my vote for the reason that I did not then have time to look into the authorities. Since that time I have taken the pains to examine the authorities upon the question presented by the appellant and I now dissent from the conclusions of the majority opinion, and vote to grant the reconsideration prayed for.

The only question presented by the appellant, under the stipulated facts, relates to the meaning of the phrase "total net income received from all *sources* within the Philippine Islands" by the appellee as that phrase is used in section 10 of Act 2833 (March 7, 1919; Vol. 14, P. L., p. 221), as amended

by section 7 of Act 2926 (March 20, 1920; Vol. 15, P. L., p. 260.) Said section 10 provided for a tax of *two* per cent upon net incomes while said section 7 required payment of *three* per cent upon net incomes; otherwise the important part of said section (10) remains the same.

This case was decided upon the following stipulated facts:

"I.

"That plaintiff is a corporation duly organized and existing under the laws of the Kingdom of Spain, duly licensed to do business in the Philippine Islands, and maintaining its principal office in said Islands in the City of Manila.

"II.

"That defendant is the duly appointed, qualified, and acting Collector of Internal Revenue for the Philippine Islands.

"III.

"That plaintiff is the owner of several 'haciendas,' sugar and oil mills and tobacco factories located in the Philippine Islands destined to the production or manufacture of tobacco, sugar, copra, and coconut oil for sale therein and in foreign countries; and has been and is still engaged, in the Philippine Islands, in the shipping business and in the buying and selling of tobacco, sugar, copra, and oil and in

the exportation of the same, and that its business has been, and is being done mainly in the Philippine Islands.

"IV.

"That the Philippine branch of the plaintiff corporation on various dates during the year 1922 exported from the Philippine Islands a quantity of centrifugal sugar, of which ten per centum was produced and ninety purchased by it in the Philippine Islands, and which was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch; and that from such transactions on centrifugal sugar during said year 1922, the plaintiff made a profit of P114,226.80, Philippine currency.

"V.

"That, likewise, the plaintiff's Philippine branch on various dates during said year 1922, exported from the Philippine Islands a certain quantity of manufactured tobacco produced by it in the Philippine Islands which was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being likewise subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch, deriving from such transactions a profit of P296,341.19, Philippine currency.

"VI.

"That, likewise, the plaintiff's Philippine branch on various dates during the said year 1922, exported from the Philippine Islands a certain quantity of copra and a certain quantity of coconut oil, produced, purchased, or manufactured by it in the Philippine Islands, which were sold in the United States by the agency therein of the plaintiff's Philippine branch, such sales being likewise subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch, and that from such transactions on copra and coconut oil the plaintiff suffered losses amounting to P10,243.14, Philippine currency.

"VII.

"That deducting the sum of P10,243.14, the losses mentioned in Paragraph VI of this stipulation, from the sum of P410,567.99, the aggregate of the profits mentioned in Paragraphs IV and V, there remained a net profit of P400,324.85.

"VIII.

"That the said net profit of P400,324.85, together with other gains, profits, or income were accounted for by the plaintiff on its books of accounts kept in the Philippine Islands as earnings made by and accruing to the Philippine branch, thereby subjecting such profits, gains, or incomes to further

business deductions—management expenses, losses, etc.

"IX.

"That the defendant Collector of Internal Revenue, acting and pretending to act under the provisions of Act 2833 (Philippine Income Tax Law), as amended by Act 2926 livied and assessed against plaintiff a tax of three (3) per centum on the amount of the aforesaid net profits (₱400,324.85) earned by plaintiff as recited in Paragraphs IV, V, and VI hereof, in the sum of ₱12,009.75, Philippine currency.

"X.

"That on the 18th day of October, 1923, plaintiff, in order to avoid the infliction upon it of fines and penalties and the distraint of its property by defendant, did pay to defendant, under instant protest in writing, the said sum of ₱12,009.75, Philippine currency.

"XI.

"That plaintiff's protest against the payment of the aforesaid tax was overruled and denied by defendant on the 20th day of October, 1923, and defendant has refused, and still continues in his refusal, to return to plaintiff, on demand, the said sum of ₱12,009.75, Philippine currency, or any part thereof.

"XII.

"That the parties hereto reserve the right to introduce evidence, direct or rebuttal, on any point not herein stipulated and which may be deemed material and necessary for the proper determination of this case."

That part of said section 7, important for this decision, provides that:

"Sec. 7. Section ten (a) of the same Act (Act 2833) is hereby amended to read as follows:

" 'Sec. 10. (a) There shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding calendar year from all sources by every corporation, joint-stock company, partnership, joint-account (cuenta en participación), association, or insurance company, organized in the Philippine Islands, no matter how created or organized, but not including duly registered general co-partnerships (compañias colectivas), a tax of three per centum upon such income; and a like tax shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding calendar year from all sources within the Philippine Islands by every corporation, joint-stock company, partnership, joint-account (cuenta en participación,) association or insurance company, organized, authorized or existing under the laws of any foreign country, including interest on bonds, notes or other interest bearing obligations of residents, corporate or otherwise, and including the income derived from

dividends or net profits subject to the tax established in this subsection.' "

From a careful reading of said section 7 it will be seen that a tax "upon the total net income" is imposed upon all classes of entities, each class including exactly the same kind of commercial entities. They are (a) domestic corporations, etc., and (b) foreign corporations, etc., doing business within the Philippine Islands. The first class is required to pay the tax upon the total net income received "from all sources", while the second class is required to pay the tax upon the total net income received "from all sources within the Philippine Islands." From the provisions of said section it at once becomes evident that it was not the intention of the legislature to collect taxes from foreign corporations on income "from sources without the Philippine Islands." From the provisions of said section it is evident that the legislature did not intend to collect taxes upon incomes received by foreign corporations from their business or branches of business outside of the Philippine Islands. The legislature of the Philippine Islands under said section did not presume that it had authority to collect taxes upon the income of foreign corporations received from sources without the Philippine Islands.

We have then the question squarely presented: What is the meaning, scope and effect of the phrase used in said section, "from all sources within the Philippine Islands?" While we have been unable to find any judicial interpretation of that phrase,

happily we have found an interpretation of the phrase by those who are authorized to speak upon that question.

In 1916 (September 8, 1916) the Congress of the United States adopted "an Act to increase the revenue and for other purposes". (Vol. 39, part I, U. S. Stat. at Large, p. 756.) Section 10 of that Act is in exactly the same language (except as to the rate of taxation) as section 7 of Act 2926. Said section contained the phrase "the total net income received from all sources within the United States" as applied to foreign corporations. In the said Act of 1916 the phrase "from all sources within the United States" was first used by Congress. The phrase used in the Act of Congress of 1913 was "business transacted and capital invested within the United States." Congress, for some reason or other, found it advisable to change the phrase "business transacted and capital invested within the United States" to the phrase "from sources within the United States." By the Act of Congress of October 3, 1917, (Vol. 40 U. S. Stat. at Large, p. 303) the term "net income" as applied to foreign corporations, is defined to mean, "the net income received from sources within the United States." (See also the Revenue Act of Congress for the year 1918.)

A question arose in the Revenue Department of the United States concerning the meaning of the phrase "from sources within the United States" as used in the Act of Congress of 1916. That question

was referred to the Attorney-General of the United States (32 Opinions of the Attorney-General of the United States, p. 336). After a careful consideration of the meaning of said phrase the Attorney-General said:

"No income is derived from the mere manufacture of goods; before there can be income there must be sale; and there is no income from sources 'within the United States from goods manufactured here (United States) unless there is, in the language of the statute, both manufacture and disposition of goods within the United States'. The purpose of the 1918 statute is to tax only income that accrues within the United States. Congress does not attempt to tax profits arising from goods manufactured in this country but sold after being shipped abroad, without being disposed of by the owner in this country (United States). When the corporation manufactures or partially manufactures articles in this country (United States), but does not sell them until they are taken abroad, there is no income 'from sources within the United States.' For the reasons given it is concluded that income which may accrue to a foreign corporation by the sale of merchandise purchased in the United States, but sold outside of the United States, is not income from 'sources within the United States.' "

That ruling by the Attorney-General was immediately accepted and followed as a correct interpretation of the phrase "from sources within the United States" by the Revenue Department of the Uni-

ted States Government; and not only that, but the same interpretation was followed in a later opinion of the Attorney-General of the United States, holding that the interpretaton given by the Attorney-General under the Act of 1916 was a correct interpretation of the use of that phrase in the Acts of Congress of 1921 and 1924. (Jan. 21, 1924, 34 Opinions of the Attorney-General of the United States, 93; 5 Treasury Bulletin, 1-39-519; Holmes Federal Taxes, 6th Ed., p. 416.)

The opinions of the Attorney-General and the regulations issued in accordance therewith, by the Treasury Department of the United States were followed until 1921, when by an Act of Congress of November 23, 1921 (Vol. 42, Part I U. S. Stat. at L., p. 227), entitled "An Act to reduce and equalize taxation, to provide revenues, and for other purposes" and in subsection (e) of section 217 of that Act, an apportionment was provided of incomes derived partly within and partly without the United States. Said subparagraph (e) provided that "items of gross income, expenses, losses and deductions, other than those specified in subdivisions (a) and (e) of said section (217) shall be allocated or apportioned to sources within or without the United States under rules and regulations prescribed by the Commissioner with the approval of the Secretary (of the Treasury). Where items of gross income are separately allocated to 'sources within the United States' there shall be deducted the expenses, losses and other deductions properly apportioned or allocated thereto

and a ratable part of other expenses, losses or other deductions which cannot definitely be allocated to some item or class of gross income. In the case of gross income derived from sources partly within and partly without the United States, the net income may first be computed by deducting the expenses, losses or other deductions apportioned or allocated thereto and a ratable part of any expenses, loses or other deductions which cannot definitely be allocated to some item or class of gross income; and the portion of such net income attributable to sources within the United States may be determined by processes or formulas of general apportionment prescribed by the Commissioner with the approval of the Secretary. Gains, profits and income from (1) transportation without the United States, or (2) from the sale of or other services rendered partly within and partly personal property produced (in whole or in part) by the taxpayer within and sold without the United States, or produced (in whole or in part) by the taxpayer without and sold within the United States, shall be treated as derived partly from sources within and partly from sources without the United States. Gains, profits and income derived from the purchase of personal property within and its sale without the United States or from the purchase of personal property without and its sale within the United States *shall be treated as derived entirely from the country in which sold.*" (Subsection (e), section 217 of Act of Congress of November 23, 1921.)

It will be noted that this section provides that

all "gains, profits and income derived from the purchase of personal property within and its sale without the United States shall be treated as derived entirely from the country in which *sold.*" Thus, the opinion of the Attorney-General, quoted above, is followed and ratified by said Act of Congress of 1921.

Subsection (e) of section 217 of the Act of Congress of November 23, 1921 (42, Part I. U. S. Stat. at L., p. 244) was carried forward and made subsection (e) of section 217 of the Act of Congress of June 2, 1924, with some changes in the last two lines. (43, Part I, U. S. Stat. at L., p. 74.)

Said subsection (e) of Section 217 of the Act of Congress of 1921 was amended in subsection (e) of section 217 of the Act of Congress of 1924 in the following manner. In the last two lines the language in the Act of 1921 was "shall be treated as derived entirely from the country in which sold", whereas the last two lines of subsection (e) of section 217 of the Act of 1924 read: "derived entirely from sources within the country in which sold." Again, it will be seen that the Congress of the United States in both of said subsections (e) adhered to the doctrine announced by the Attorney-General in Vol. 32, Opinions of the Attorney-General of the United States, p. 336, providing expressly that "gains, profits and income derived from the purchase of personal property within and its sale without the United States or from the purchase of personal property without and its sale within the United States, shall

be treated as derived entirely from sources within the country in which *sold*."

THE INCOME IN QUESTION, BY THE STIPULATED FACTS AND BY THE ADMISSION OF THE ATTORNEY-GENERAL IN THIS COURT, WAS DERIVED FROM MERCHANDISE SOLD IN THE UNITED STATES

Considering the similarity of the statute here and the Acts of Congress of 1916, 1917, 1918, 1921 and 1924, and the meaning of the phrase "total net income received from all sources within the United States" (total net income received from all sources within the Philippine Islands) as interpreted not only by the highest fiscal department in the United States and followed by the Revenue Department, but by the Congress of the United States, to wit: that "no income is derived from the mere manufacture of goods; before there can be income there must be sale; and there is no income from 'sources within the United States' from goods manufactured in the United States unless there is, in the language of the statute, 'both manufacture and disposition of the goods within the United States'. The purpose of the 1916 statute is to tax only income that accrues within the United States. Congress does not attempt to tax profits arising from goods manufactured in this country but sold after being shipped abroad without being disposed of by the owner in this country (United States). When a foreign corporation manufactures or partially manufactures articles in this country (United States) but does not sell them until

they are taken abroad, there is no income 'from sources within the United States.' "

From the foregoing we are led to the question, where were the merchandise involved in this question sold? We find the answer to that question (1) in the stipulated facts (paragraphs 4, 5, 6 of the stipulated facts) and (2) in the brief of the Attorney-General (p. 6). Said paragraphs of the stipulated facts expressly provide that the merchandise from which the income in question arose "*was sold in the United States.*" The Attorney-General in his brief, at page 6, also makes the statement that: "It is true that the sale of the articles was made in the United States." In our opinion it would be a great injustice to the appellee if the stipulation presented at the beginning of the trial and the admission of the Attorney-General after the trial should be construed now to the prejudice of the appellee. We do not believe, in view of said stipulation and admitted fact by the Attorney-General, that any question should be raised at this time as to the place of the sale. The question of the place of the sale has been admitted to be in the United States.

It is argued, however, in the majority opinion that inasmuch as the sale was by an agent in the United States, "the sale being subject to confirmation, etc., as to price and other terms and conditions," that the sale was not made in the United States according to the stipulated facts, but was made in fact in the Philippine Islands. We cannot give our assent to that argument. The sale took place, by agree-

ment of the parties, where the goods were, in the United States at the time of the sale.

We must not confuse the source of property with the source of income from property.

The taxing power of the Philippine Islands does not extend beyond its territorial limits. The Philippine Government has no authority to tax property nor an income from property beyond its territorial limits. The Legislature evidently recognized the limitation of its powers when it provided in section 10 above quoted for a tax upon "the total net income received from all sources *within* the Philippine Islands."

The place where the sale of personal property takes place is always a question of fact, depending upon the facts and circumstances of each particular case. A few examples may serve to illustrate:

First Example: "A" is a manufacturer or producer of hats in the city of Manila. He has an agent in the city of Dagupan. He sends hats from time to time to his agent to be sold in Dagupan. The place of sale in this example is evidently Dagupan and not Manila.

Second Example: "A" is a manufacturer of hats in the City of Manila. "B", a citizen of Dagupan, orders a number of hats to be sold by him on his own account as a merchant in the city of Dagupan. The entire transaction takes place in the city of Manila. In this case the sale of the hats takes place in the city of Manila.

Third Example: "A" is a manufacturer of

hats in the city of Manila. "B" orders a number of hats from "A" to be delivered and paid for at the city of Dagupan. In such a case the sale takes place at the city of Dagupan and not in the city of Manila.

Fourth Example: "A", a manufacturer of hats in the city of Manila, entered into a contract with "B" to deliver a quantity of hats in good condition in the City of New York. The hats were damaged in transit. The sale was not complete until the hats were delivered in good condition in the city of New York. The sale was made in the city of New York and not in the city of Manila. (McCullough & Co. vs. Berger, 43 P. R., 823; 35 Cyc., pp. 274, 275, 276.)

Fifth Example: "A" is a manufacturer of hats in the city of Manila. He has an agent in the city of San Francisco to whom he sends large quantities of hats to be sold by his agent. "A" reserves the right to fix the price and conditions of the sale from time to time, as well as to confirm all sales. The hats were sold by the agent in San Francisco in accordance with the arrangement with "A". The sale is made in the United States.

Sixth Example: "A" is a foreign corporation doing business in the Philippine Islands and is a manufacturer and purchaser of hats in the city of Manila. From time to time he ships his products to the city of San Francisco in the United States to be sold there. He has a bodega or store in San Francisco. From time to time he goes to the United States and personally, as opportunity presents itself, sells said merchandise in the United States. The

sale is made in the United States, notwithstanding the fact that his books of account concerning the purchase, manufacture and sale of said hats are kept in the branch office in the city of Manila.

THE FACT THAT THE SALE IN THE UNITED STATES WAS SUBJECT TO CONFIRMATION BY THE PHILIPPINE BRANCH DOES NOT MAKE THE SALE ONE IN THE PHILIPPINE ISLANDS.

The fact that the Philippine branch of the plaintiff corporation reserved the right to control its agent in the United States in the sale of merchandise in question does not make the sale, a sale within the Philippine Islands. The sale was made in the United States as per the stipulated facts and admission of the Attorney-General. The control of the sale as to price, etc., does not change the *place* of the sale of the merchandise. The Philippine branch of the plaintiff corporation simply took the precaution of having full control of the acts of its agents in the United States. The condition would have been exactly the same had the principal accompanied the merchandise to the United States and sold it. The sale by the agent does not change the place of sale. Corporations can only act through their agents.

THE PLAINTIFF IS SUBJECTED TO DOUBLE TAXATION

Under the stipulated facts the plaintiff is doing business in the United States. It has an income from said business. Under the Acts of Congress of 1916-24 it is subject to pay an income tax upon the "gains, profits and income derived from the purchase of personal property without the United

States" and under the decision of the majority opinion, he is also required to pay a tax upon the same income in the Philippine Islands. He is therefore subjected to a double tax on the same income.

Under the doctrine of the majority opinion the plaintiff, as a foreign corporation, bears an unequal burden to that imposed upon domestic corporations, notwithstanding the fact that it was the "purpose, and intent of the Legislature that a foreign corporation which has a branch office in the Philippine Islands and engaged in business here should pay the same amount of income tax on that business as a domestic corporation."

DOMESTIC AND FOREIGN CORPORATIONS SUBJECTED TO UNEQUAL BURDEN.

If the doctrine of the majority opinion is the correct interpretation of the law, then domestic and foreign corporations are subjected to unequal burden in accordance with the provisions of paragraphs (a) and (b) of section 12 of Act 2833. Their allowable deductions are not the same.

It is well established that a state, or territory authorized to legislate for itself, may regulate the activities of foreign corporations within the state or such territory, but it cannot regulate or interfere with what foreign corporations may do outside.

The plaintiff was authorized, through its branch office, to do business in the Philippine Islands. If it chose to do business outside of the Philippine Islands it had a perfect right to do so and the Philippine Legislature has no authority to place a burden

upon the business done outside of the Philippine Islands.

Allgeyer vs. Lousiana, 165 U. S. 578
St. Louis Compress Co. vs. Arkansas, 260 U. S. 346
Compañía General de Tabacos de Filipinas vs. Coll. of Int. Rev., decided by the Supreme Court of the U. S., Nov. 21, 1927.

In my opinion the motion for reconsideration should be granted and the judgment appealed from should be affirmed.

E. FINLEY JOHNSON.

STREET, *J.*, *dissenting*:

Although I signed the original opinion in this case I am constrained, upon further reflection, to record the belief that the assent thus given to the decision was ill-advised,—a mistake apparently due to an erroneous perception of the bearing upon this case of the two opinions of the Attorney-General of the United States and certain Congressional legislation referred to in the dissenting opinion of Mr. Justice Johnson. In dealing with a statute adopted by the Philippine Legislature from an Act of Congress we should be careful to take the law with the interpretation placed upon it by competent authority in the United States; and special care should be taken about this in dealing with the intricate matters covered by the income-tax laws. Our endeavor should be to cooperate, as far as possible, with the Revenue

Department of the United States, in making the operation of these laws just and uniform.

The opinions of the Attorney-General of the United States to which reference has been made sustain the proposition that when merchandise is purchased or produced in one country and sold in another, the place of sale is to be taken as the place of the source of income for the purpose of applying a law such as is under consideration in this case; and it will be noted that the ruling thus made arose upon facts where the conclusion reached was contrary to the interests of the Government revenue,—a circumstance which indicates that probably no strong considerations in favor of the Government were overlooked. In addition to this subsequent legislation of Congress, while accepting said proposition as a general rule, has defined the particular cases where a different rule shall be applied. But in the Philippine Islands we have none of this supplemental legislation, with the result that the rule enunciated by the Attorney-General is applicable in its full extension in this jurisdiction, not of course as a binding rule of law but as a competent interpretation of the statute from which our own law is taken.

My conclusion is in conformity with that reached by Mr. Justice Johnson, namely, that the decision heretofore entered in this case should be set aside and the appealed judgment affirmed.

THOS. A. STREET.

On February 9, 1928 the Clerk of the Supreme Court of the Philippine Islands entered the final judgment which reads as follows:

[CAPTION OMITTED]

The Court having regularly acquired jurisdiction for the trial of the above-entitled cause submitted by both parties for decision, after consideration thereof by the Court upon the record, its decision and order for judgment having been filed on the 6th day of December, A. D. nineteen hundred and twenty-seven;

By virtue thereof it is hereby adjudged and decreed that the judgment of the Court of First Instance of Manila, dated the 16th day of November, nineteen hundred and twenty-six, and from which the above-entitled appeal was taken, be, and the same is hereby, reversed and the complaint dismissed, with costs for the defendant.

It is further ordered that the appellant recover from the appellee the sum of P40.00 as costs.

(Sgd.) V. ALBERT
Clerk of the Supreme Court of the Philippine Islands.

I, V. ALBERT, Clerk of the Supreme Court of the Philippine Islands, do hereby certify that the foregoing final judgment was entered in the record on February 9, 1928.

V. ALBERT
Clerk of the Supreme Court of the Philippine Islands.

On February 14, 1928, the plaintiff and appellee filed the following exception and notice of intention to petition for a writ of certiorari:

[CAPTION OMITTED]

Comes now the appellee in the above entitled case, by its undersigned attorneys, and hereby excepts to the order promulgated by this Honorable Court on the 8th day of February, 1928, overruling its motion for reconsideration of the decision theretofore rendered in this case, and also excepts to the final judgment entered herein, and hereby gives notice of its intention to apply to the Supreme Court of the United States for a writ of certiorari for the review of the decision and judgment of this Court entered in this cause, and respectfully requests that the record of this cause be retained in this Court pending the preparation of the petition and of the record to accompany the same.

Manila, P. I., Febraury 14, 1928.

DEWITT, PERKINS & BRADY,
By: WILLIAM C. BRADY,
Attorneys for the appellee,
601 Pacific Bldg., Manila.

On February 16, 1928, the defendant and appellant filed the following opposition:

[CAPTION OMITTED]

Comes now the undersigned on behalf of the defendant-appellant in the above-entitled case and opposes the petition of February 14, 1928 of the plaintiff-appellee herein, for the reason that there is no ground for appealing this case to the Supreme Court of the United States by writ of certiorari inasmuch as there is no question in this case involving the Constitution or any statute, treaty, title, right or privilege of the United States and the value in controversy does not exceed $25,000.

Manila, February 16, 1928.

DELFIN JARANILLA,
Attorney-General.

On the same date, to wit, February 16, 1928, the Supreme Court issued the following order:

Considering the motion of the attorneys for the appellee in case R. G. No. 27766, Compañía General de Tabacos de Filipinas vs. Collector of Internal Revenue, excepting to the order of this Court overruling the appellee's motion for the reconsideration of the decision heretofore rendered therein and to the final judgment entered in said case, and giving notice of appellee's intention to apply for a writ of certiorari to the Supreme Court of the United States of Amer-

ica for the review of said decision and judgment, and praying that the record of said case be retained in this Court pending the preparation of the application for a writ of certiorari and of the proceedings to be had in the Supreme Court of the United States: Exception noted and the amount of the bond for the stay of the execution of judgment is hereby fixed at ₱1,000.00 to be filed with this Court within ten days from notice hereof and to be approved by Mr. Justice Johns, after hearing the defendant as to the sufficiency of the same and as to the solvency of its

In due time the bond was filed with the Supreme Court and duly approved by the Honorable Charles A. Johns, Associate Justice of said Court.

United States of America

PHILIPPINE ISLANDS

In the Supreme Court of the Philippine Islands

I, V. ALBERT, Clerk of the Supreme Court of the Philippine Islands, do hereby certify that the foregoing 63 printed pages contain a true and correct translation and transcript of the record of the case entitled Compañía General de Tabacos de Filipinas, plaintiff and appellee, *versus* Collector of Internal Revenue, defendant and appellant, bearing No. 27766 of the docket of this Supreme Court.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of this Court this ... day of June, one thousand nine hundred twenty-eight.

V. ALBERT,
Clerk of the Supreme Court
of the Philippine Islands.

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 22, 1928

The petition herein for a writ of certiorari to the Supreme Court of the Philippine Islands is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.